

**IN THE COURT OF COMMON PLEAS OF THE STATE OF DELAWARE**  
**IN AND FOR NEW CASTLE COUNTY**

HARFORD CHEMICAL GROUP, LLC	)	
Plaintiff	)	
	)	
v.	)	C.A. No: U407-03-270
	)	
HENRY W. JARUSIK,	)	
Defendant	)	

Date Submitted: July 28, 2009  
Date Decided: August 12, 2009

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**DECISION AFTER TRIAL**

This is an action brought by Plaintiff Harford Chemical Group, LLC (“Harford”) to recover a total of \$40,500 in payments (“the payments”) made by Harford to Defendant, Henry W. Jarusik (“Jarusik”), one of its partners. Harford claims that the payments were loans to Jarusik. Jarusik contends that the payments constituted salary, not loans. Trial was held on July 28, 2009 and this is the Court’s final decision.

### **Facts:**

In May 2004, David Potter (“Pottter”), then a chemical engineer working for Northway Chemicals (“Northway”), formed Harford as a Limited Liability Company (LLC). The business plan for Harford was to import specialty chemicals from China and sell them to various U.S. corporations. At the time, Jarusik was employed as the Chief Financial Officer (“CFO”) of Northway. Potter and Jarusik discussed collaborating on the Harford venture, and in June 2004, Jarusik quit his job with Northway to devote full-time work to Harford. Potter continued working part-time with a consulting firm and also devoted work to Harford.

Potter and Jarusik hired an attorney to redraft the original LLC Agreement.<sup>1</sup> The Agreement provided that Potter and Jarusik were both 50% owners and each contributed \$10,000 to the company. Jarusik was to handle the finances for Harford, which included preparation of financial statements and invoices, paying bills, and banking.

The Harford venture was not successful financially. In 2004, no sales were made, and in 2005, approximately \$1,600 in sales was made. At some point, the company contemplated receiving a loan from Potter’s wife, and loan documents were prepared. During the 2004 calendar year, Jarusik issued eight checks from the Harford business account to himself, totaling \$28,500.<sup>2</sup> During the 2005 calendar year, Jarusik issued three

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<sup>1</sup> Potter testified that Harford spent \$6,000 towards preparation of the Agreement, which involved extensive meetings and negotiations, particularly regarding succession planning for the company.

<sup>2</sup> The 2004 checks were introduced into evidence as Plaintiff’s Exhibit 4. The chart below reflects the contents of the checks:

<u>Date:</u>	<u>Amount:</u>	<u>Memo Line:</u>
9/9/04	\$4,000	(blank)
9/24/04	\$5,500	payroll advance 7/04
10/12/04	\$5,000	payroll adv 8/04
10/27/04	\$1,000	pyrl

checks, totaling \$12,000.<sup>3</sup> At some point after that, Potter demanded that Jarusik repay the \$40,500 to Harford, stating that the payments were loans, rather than salary. Jarusik refused to repay the amounts, and resigned from the company in April, 2005. Potter subsequently attempted to continue running the business and later resigned as well.

Potter testified that he and Jarusik had an understanding that the payments were to be loans because guaranteed payments were not to take place until the company started making money. Potter further testified that he had never taken any payments from Harford, and that he and Jarusik had never discussed guaranteed payments. Jarusik's recollection was that he and Potter did discuss Jarusik's salary; that Potter knew that Jarusik gave up his employment and would have no income after joining Harford; and that he was looking for a salary of \$90,000.

There was never any written agreement as to how Potter or Jarusik would be compensated. No loan documents or promissory notes were executed. Plaintiff contends that the payroll statements, financial statements, tax returns, and checks prepared in 2004 show that the payments were loans rather than salary. Because there was no accounting for the year 2005, Harford's claim for the \$12,000 paid to Jarusik in 2005 is based solely on the checks introduced into evidence.

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11/5/04	\$4,500	pyrl
11/18/04	\$1,500	pyrl
12/6/04	\$5,000	pyrl adv 11/04
12/21/04	\$2,000	june bal due

<sup>3</sup> The 2005 checks were introduced into evidence as Plaintiff's Exhibit 5. The chart below reflects the contents of the checks:

<u>Date:</u>	<u>Amount:</u>	<u>Memo Line:</u>
1/5/05	\$5,000	(blank)
2/14/05	\$5,000	(blank)
3/10/05	\$2,000	(blank)

Harford introduced into evidence a number of documents which, it contends, show that the payments were loans rather than salary. Plaintiff's Exhibit 1 is Harford's annual Federal Unemployment Tax Return (FUTA) Form 940 for 2004. Plaintiff's Exhibit 2 is Harford's Quarterly Tax Return Form 941 for 2004. Both forms were prepared by Jarusik and/or an accountant and signed by Jarusik. Harford points to the fact that neither form reports any wages paid in 2004. In response, Jarusik testified that the payments did not have to be reported, because Jarusik was a partner not an employee.

Harford also points to financial statements for the company to suggest that the payments were loans. Plaintiff's Exhibit 9, an income statement for Harford, classifies the payments (\$28,500) as "Loans & Exchanges" under the "Liabilities" header. Similarly, Defendant's Exhibit 1, a spreadsheet of expenses for Harford, lists the individual 2004 checks under the "Loans & Exchanges" header. In response, Jarusik testified that the "Loans & Exchanges" section was a logical place to file the payments under the accrual basis system, and that the payments were "exchanges" not "loans."

Harford also submitted Plaintiff's Exhibit 3, a copy of Harford's U.S. Return of Partnership Income for 2004. In that document, the payments are listed under Statement 4, "Other Assets," and labeled as "Partner Advance." Harford argues that if the payments were loans, they should have been listed under Statement 3 of the form under "Prepaid Expenses." In response, the defense points to the fact that Line H of the form ("Check accounting method"), indicates that the accrual method of accounting was used rather than the cash method. Jarusik also testified that he managed Harford's finances on an accrual basis rather than a cash basis. He further explained that under the accrual basis, expenses are recognized in the period in which related revenue is recognized. In terms of

accounting, the payments can be removed from the “assets” column of the balance sheet and placed in the “expenses” column of the balance sheet once the company starts to generate income. Because Harford was not recognizing any income at the time the checks were issued to Jarusik, he classified the payments as assets, rather than expenses.<sup>4</sup>

Jarusik testified that he interfaced with the accounting firm retained by Harford in the preparation of the reports and returns introduced as exhibits.

### **Analysis**

The plaintiff in a civil suit is required to prove all the elements of its claim by a preponderance of the evidence.<sup>5</sup> For the reasons below, the Court finds that Plaintiff has not satisfied this burden.

There exists no written agreement stating the payments at issue were loans. Plaintiff relies on a series of tax returns, financial statements, spreadsheets, and checks to bolster its claim that the payments were loans rather than salary. Yet for every argument that the Plaintiff has presented based on these documents, the Defendant has submitted an equally persuasive explanation as to why the payments were not loans. The contents of the tax returns and financial statements comport with the Defendant’s position in light of Jarusik’s explanation of the accrual based accounting system. Plaintiff has not presented sufficient evidence to cast doubt on this. The checks submitted into evidence do not aid the Court in determining the nature of the payments, as none of the checks are labeled as “loans.” Significantly, most of the checks have notations of “payroll” on the check or stub.

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<sup>4</sup> Potter testified on cross examination that Harford did not make any sales during 2004, and made approximately \$1,600 in sales during 2005.

<sup>5</sup> *Reybold Group, Inc. v. Chemprobe Technologies, Inc.*, 721 A.2d 1267 (Del. 1998)

In addition, the underlying circumstances of the parties during the time at issue belie the proposition that these payments were loans. First, it is clear that Potter and Jarusik handled other matters with great care and attention to detail. For example, Potter testified that he and Jarusik engaged in several meetings and negotiations with their attorney in order to carefully draft the LLC Agreement. Also, when Potter's wife was contemplating providing a loan to the company, loan documents were prepared. In light of these facts, it appears that if these payments were expected to be repaid to the company, they would be based on more than a vague "understanding." Second, the Court finds it significant that Jarusik left his job as a CFO with Northway, which paid him an annual salary of \$90,000. It makes little sense for someone to leave such a well-paying job to work for loans. Third, apparently no serious objection to the payments as salary was made until after all the checks had been issued.

For the foregoing reasons, Judgment is entered for the Defendant. Each party shall bear their own costs.

**SO ORDERED**

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Alfred Fraczkowski  
Associate Judge<sup>6</sup>

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<sup>6</sup> Sitting by appointment pursuant to Del. Const., Art. IV, §38 and 29 Del. C. §5610.